United States Court of Appeals

for the Second Circuit

PETITION FOR REHEARING AND SUGGESTION FOR REHEARING EN BANC

74-1243

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Trans World Airlines, Inc.,

Plaintiff-Appellee,

-against-

Howard R. Hughes, Hughes Tool Company and Raymond M. Holliday,

Defendants-Appellants.

Appeal From The United States District Court

For The Southern District of New York

PETITION FOR REHEARING AND SUGGESTION FOR REHEARING IN BANC

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Preliminary Statement

Plaintiff-Appellee Trans World Airlines, Inc. ("TWA") respectfully petitions for rehearing, and suggests the appropriateness of rehearing in banc, of the decision in the above entitled case by a panel of this Court (Moore, Oakes and Timbers, Circuit Judges) on March 7, 1975, Slip Opinion, pp. 2085-2098.

In an opinion by Judge Oakes, joined in by Judge Moore, the Court

(1) reversed so much of an order of the United States District Court for the Southern District of New York, Metzner, U.S.D.J., as disallowed $683,805.40 out of a total of $1,872,453.15 in costs taxed by the clerk in favor of defendants-appellants and against TWA, representing $617,765 for accountants' fees incurred in providing quarterly audit reports with respect to the net worth of defendant-appellant Hughes Tool Company,* and $66,060.40 for charges incurred (in addition to the $1,015,625 commitment fee allowed by the district court) in providing security to the Bank of America for a $75 million letter of credit in lieu of a supersedeas bond, and

(2) affirmed so much of the district court's order as allowed to TWA a setoff of $4,602.55 against the costs taxed, representing the expenses incurred by TWA in preparation for a deposition of Howard R. Hughes which was precipitously cancelled by a last-minute announcement that Hughes would not appear.

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* Defendant Hughes Tool Company changed its name to Summa Corporation late in 1972, but here, as in the past we will refer to it as "Toolco," and to defendants-appellants Toolco and Raymond M. Holliday collectively as "defendants".

Judge Timbers filed a separate opinion dissenting from that part of the Court's decision which reversed the district court's disallowance of the $617,765 item for quarterly audits, stating that there was no showing that the trial judge had clearly abused his discretion in disallowing taxation of this item as costs against TWA.

Reasons for Granting the Petition

The reasons for seeking rehearing and suggesting rehearing in banc, are that:

(a) The Court's decision erroneously substitutes the judgment of the appellate court for that of the district court in an area where reviewing courts have universally deferred to the judgment of the trial court in the absence of a clear abuse of discretion; and

(b) In light of the relatively infrequent opportunity for appellate courts to speak on the subject, the Court's decision here will certainly be taken as controlling in this Circuit (and influential elsewhere) for years to come in the area of taxing costs for providing security for a stay pending appeal. Since the effect of the decision is to deprive the trial court of discretion to withhold the allowance of costs incurred by defendant but which the court considers

unnecessary or unreasonable, it is respectfully submitted that it would be particularly appropriate for this Court to have an opportunity to consider this important issue in banc, before the decision becomes binding on the lower courts under its supervision.

Argument

As Judge Timbers suggests in his dissenting opinion, prior to the Court's decision on this appeal it had seemed to courts, commentators and litigants alike that "[t]here are few areas where * * * it was more axiomatic that the exercise of discretion by a trial judge should not be disturbed absent the clearest showing of abuse than in the taxation of costs" (Slip Opinion, p. 2094). Without unnecessary multiplication of authorities, it is evident that this has been the universal view. See, e.g., Farmer v. Arabian American Oil Co., 379 U.S. 227, 235-36 (1964); McDonnell v. American Leduc Petroleums, Ltd., 456 F.2d 1170, 1188 (2d Cir. 1972); Oscar Gruss & Son v. Lumbermens Mutual Casualty Co., 422 F.2d 1278, 1284-85 (2d Cir. 1970); 10 Wright & Miller, Federal Practice & Procedure: Civil § 2688 (1973).

The present decision, however, carves out an exception to this general rule. With respect to taxation of costs, the Court appears to contemplate a de novo review in every case of a trial court's exercise of discretion when the particular items of cost allowed or disallowed relate to a prevailing defendant's provision of security for a stay pending appeal. This exception seems to be premised upon the language of Fed.R.App.P. 39(a) and (e).* Although the Court's opinion does not expressly state that the words "shall be taxed" in Rule 39 leave to the district court only the ministerial function of computing the amount of premiums paid for a supersedeas bond and entering a judgment for costs in that amount, the possibility that the Court's decision is subject to such a construction - and we are aware of no decision or commentary which so interprets the Rule - is of itself a matter of sufficient import to suggest the desirability of a rehearing to clarify the Court's meaning.

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* The Court's consideration of the issue is introduced with the following:

> "However costs on appeal have been treated in the past * * *, they are now governed by Fed.R. App.P. 39(a) and (e). Under Rule 39(a), 'Except as otherwise provided by law . . . if a judgment is reversed, costs shall be taxed against the appellee unless otherwise ordered. . . ." Under Rule 39(e) 'the premiums paid for cost of supersedeas bonds or other bonds to preserve rights pending appeal . . . shall be taxed in the district court as costs of the appeal in favor of the party entitled to costs under this rule.'" (Slip Opinion, pp. 2087-2088)

The Court's opinion reviews at some length the proceedings which led the district court to permit defendants to provide a $75 million letter of credit and maintain Toolco's net worth at three times the remainder of the judgment (which the audited quarterly financial statements were designed to demonstrate) in lieu of a supersedeas bond in the full amount of the judgment as contemplated by Fed.R.Civ.P. 62(d) and S.D.N.Y. Gen.R. 33 (Slip Opinion, pp. 2088-2091). It is with the Court's conclusion based upon that review that we respectfully take issue.

The Court's opinion states:

> "In our view the costs of the audits under the consent order were costs in lieu of providing a supersedeas bond as provided by the rules. Just as the court allowed the one-half of one per cent premium on the letter of credit, so too it should have allowed the costs for the audits." (Slip Opinion, p. 2091; footnote omitted)

Thus the majority finds Judge Metzner's refusal to allow the audit costs to be an abuse of whatever discretion he had, commenting that it was "exercised arbitrarily" since "no criterion" was set forth. (Slip Opinion, p. 2092) Since Judge Metzner's action was taken only after extensive consideration and review of the proceedings involved in the entry of the stay - proceedings lasting for nearly four months and involving

repeated in camera hearings - we are constrained to believe that the majority has overlooked the real basis for Judge Metzner's decision.

It is clear from the record that Judge Metzner decided at the very outset that the defendants, to protect their right of appeal, would be granted a stay of the judgment on terms which would permit them (as they plainly desired) to carry on their business as usual. He at no time suggested that this was an improper motivation. At the same time however he was concerned to provide for the plaintiff's right to adequate security for the judgment in its favor.

The crux of the problem was that Toolco, although admittedly amply able to pay the judgment at the time of the hearings in 1970, was known to the court to be the creature of its sole stockholder, the defendant Howard Hughes, over whom the court had no personal jurisdiction and who was, indeed, probably beyond the reach of any United States court. The danger was that the assets of Toolco would be disposed of on Hughes' instructions in such a manner as to preclude collection of the judgment. The problem was to provide reasonable assurance against this happening on a basis that would not preclude "business as usual" by the defendants, if that was what they desired.

There were numerous ways in which this could be done. Some of them, urged by TWA, would have been practically cost-free. TWA asked for a mandatory restriction on disposition of assets not in the usual course of business, or for a limitation on dividends (a limitation of $5 million a year in excess of whatever amount was needed by Hughes to pay taxes on Toolco's income* was tentatively suggested, and TWA expressed a willingness to accept a higher amount if Toolco would suggest one). These requests were refused by defendants. TWA suggested that Hughes could individually subject himself to the jurisdiction of the court, solely for purposes of securing the judgment, so that his responsibility for any unwarranted dispersal of assets could be enforced. Alternatively the suggestion was made that his stock in Toolco could be pledged as security for the judgment, so that dividends paid upon that stock might be recovered if they left Toolco unable to pay the judgment.

All such suggestions were rejected. The only assurance defendants were willing to offer was such assurance as would be available through quarterly audited financial statements that the feared disposition of assets had not taken place. This assurance, unsatisfactory as it was, was

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* Toolco's very substantial income, since Toolco is a "subchapter S corporation," is taxable in its entirety directly to Hughes as Toolco's sole stockholder.

also the source of the $617,765 of costs which the majority of the Court has held must be allowed since it was in lieu of providing a supersedeas bond, and it cost less than such a bond would have cost (Slip Opinion, p. 2092).

The conclusion which Judge Metzner reached below, however, was that Toolco acted unreasonably in insisting on this method, and only this method, of providing security, when cost-free alternatives were available. He held that it was unfair to the plaintiff to saddle it with the expense to Toolco of doing things the way it wished to do them.

Judge Metzner was well aware that the requirement that the proposed quarterly financial statements must be audited by independent certified public accountants was inserted at the suggestion of the defendants. Indeed, TWA on two occasions expressly stated that an outside audit of the proposed quarterly financial statements was unnecessary as far as TWA was concerned, since these financial statements could be certified by a responsible financial officer of Toolco. (App. 28a; Doc. 16, p. 4 and Ex. B, p. 7).* TWA was obviously more concerned that the order contain other provisions for giving TWA reasonable assurances against improper

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* Reference herein to "Doc. 16" is to part of the original record on appeal not reproduced in the printed appendix. For the Court's convenience copies of Doc. 16 were provided to the panel by counsel for TWA at the oral argument on October 22, 1974.

acts by Hughes and Toolco. Judge Metzner was also undoubtedly aware that liens upon specific assets, pledges of various short term securities, and the like, although refused by defendants to TWA, had been provided by defendants to the Bank of America.

In the light of this history we submit that Judge Metzner's conclusion that defendants' position had been unreasonable was not only not an abuse of discretion - it was plainly right.

In fact, what the majority has done is to establish a rule of law that a defendant who provides alternate security for a stay pending appeal in lieu of the customary supersedeas bond cannot be required to do it in the most economical manner, at least as long as the method he chooses is not more expensive than the supersedeas bond would have been. Even though the court supervising the transaction considers the defendant's choice to be unreasonable and unnecessarily expensive, it may not withhold full reimbursement to the defendant of his costs in the event that his appeal is successful. As far as we are aware such a limitation upon the discretion of the trial court has never previously been suggested and we do not believe that Rules 39(a) and 39(e) of the Federal Rules of Appellate Procedure provide a statutory foundation for such a change in the prior law.

By focusing in this Petition on the quarterly audits, the larger of the two items of costs as to which the district court's disallowance was reversed by the Court, we do not mean to suggest that the district court's disallowance of the expenses incurred by Toolco in providing security to the Bank of America for the letter of credit was improper. Similar considerations with respect to the proper standard for appellate review apply as to this item. Such expenses, moreover, are plainly equivalent to the cost of providing security to a bonding company and we understand that the customary practice in the federal courts has been, while allowing the bond premium, to disallow ancillary expenses such a legal and other fees incurred in placing liens for the bonding company's benefit on real property or other assets of the defendant. If this Court is to forbid such a distinction, even as a matter of the trial court's discretion, we submit that it should only be after in banc consideration.

The Supreme Court long ago suggested that such matters are best left to "the discretion vested in the trial court * * * and the better opportunity of that court to exercise that discretion from its greater intimacy with details of the pleadings, hearings, and orders in the case." Newton v. Consolidated Gas Co., 265 U.S. 78, 83 (1924). The Court's application in this case of a less restricted standard of review is, we believe,

unwarranted, particularly since it results in imposition of substantial additional costs which the trial court supervising the proceedings found to have been unnecessary and unreasonable in the circumstances presented.

Conclusion

For the above reasons, it is respectfully submitted that rehearing or rehearing in banc of the Court's decision on this appeal should be granted and the order of the district court appealed from should be affirmed in all respects.

Dated: New York, New York
March 21, 1975

Respectfully submitted,

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